

## Current Support Brief

### CONTINUED ECONOMIC SLOWDOWN IN THE EUROPEAN SATELLITES IN 1963



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CONTINUED ECONOMIC SLOWDOWN  
IN THE EUROPEAN SATELLITES IN 1963\*

Economic growth in the European Satellites in 1963 may be even slower than in 1962, when gross national product (GNP) increased only about 2-1/2 percent. In the area as a whole, industrial production will increase considerably less than last year, and agricultural production probably will increase only slightly, equaling approximately the average level of the past 4 years. There will be little or no change in personal consumption.\*\*

Czechoslovakia is having its worst year for growth since World War II, with possibly no increase at all in industrial production and little if any increase in agricultural production. Poland also is having a bad year, with a substantially reduced rate of industrial growth and probably a drop in agricultural production. Only Rumania is having a good year, with continued rapid growth in industry and some increase in agricultural production. Some progress in intra-Bloc economic cooperation is apparent, although a Soviet attempt to move toward supranational planning in the Bloc failed because of economic nationalism in the Satellites, especially in Rumania.

The slow growth of the Satellite economies this year is a result partly of fundamental factors and partly of temporary factors, including unusually bad weather last winter. Rates of industrial growth have shown a downward trend for 3 or 4 years in the more developed Satellites, especially East Germany and Czechoslovakia, but not in the least developed countries -- Rumania and Bulgaria. The recent tendency in economic policy to stress efficiency and "production for use, not for production's sake" has been strengthened. Economic difficulties in the industrialized Satellites have forced some further changes in the system of economic management and have bred a number of proposals for improving incentives, but there are differences and confusion about the purpose and future extent of reforms.

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\* Albania is not considered in this publication.

\*\* Official data are used for industrial production and investment, and estimates of this Office are used for agricultural production and consumption.

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1. Slowdown in Industry

The growth of industrial production this year will be considerably smaller than last year in Poland and slightly smaller in East Germany, Hungary, Rumania, and Bulgaria (see the table). In Czechoslovakia, where production in the first half of 1963 was almost 2 percent below the first half of 1962, there may be no growth at all in the year as a whole compared with an increase of more than 6 percent in 1962.

Table

European Satellites: Growth of Gross Industrial Production  
and Capital Investment  
1959-63

	Annual Percentage Increases				
	<u>1959</u>	<u>1960</u>	<u>1961</u>	<u>1962</u>	<u>1963</u> <u>a/</u>
Gross industrial production					
Bulgaria	20.5	13.5	11.7	11.1	9.9 <u>b/</u>
Czechoslovakia	10.9	11.7	8.9	6.1	-1.5 <u>c/</u>
East Germany	12.6	8.2	5.9	6.2	4.4 <u>d/</u>
Hungary	9.3	12.3	10.2	8.0 <u>e/</u>	6.3 <u>f/</u>
Poland	9.2	11.2	10.3	8.3	5 <u>d/</u>
Rumania	11.1	16.9	15.6	14.7	13 <u>d/</u>
Capital investment					
Bulgaria <u>g/</u>	48.0	22.4	1.9	7.7	17.8 <u>b/</u>
Czechoslovakia	19.5	12.3	7.2	-2.6	-14 <u>b/</u>
East Germany <u>h/</u>	13.8	8.9	1.3	1.4	Negl. <u>d/</u>
Hungary	39.9	16.8	-10.1	13.7	N.A.
Poland	16.9	6.0	7.4	11.0	2.8 <u>i/</u>
Rumania	17.9	32.1	21.4	15.6	N.A.

a. Percentage increase above the corresponding period of the previous year.

b. Data are for 9 months.

c. Data are for 6 months; results for the year should be higher.

d. Official expectation for the year.

e. Net production.

f. Data are for 8 months; results for the year should be higher.

g. Centralized investment.

h. Including capital repairs.

i. Socialized investment for 7 months; results for the year should be higher.

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The recent slowdown in the more industrialized Satellites reflects a basic trend, not just temporary difficulties. Since 1960, Rumania and Bulgaria have maintained high rates of growth of 10 percent a year or better, but rates in Poland and Hungary have declined from about 10 percent to less than 7 percent and those in East Germany and Czechoslovakia have fallen to below 5 percent. Thus rates of growth at present are inversely related to the degree of industrialization in contrast to the earlier postwar period, when there was little connection between these factors. This changing relationship reflects the effect of some fundamental factors in the more industrialized countries -- the progressive exhaustion of reserves of labor and productive capacity; the deterioration of equipment in light industry, transportation, and parts of the machine building industry as a result of inadequate maintenance and replacement of plant and equipment; the inflexibility of the system of economic management in adjusting to the increasingly complicated pattern of both internal and external demand; and the stagnation of agricultural production, which has led to increased imports of food at the expense of imports supporting industrial growth.

These problems are most severe in East Germany and Czechoslovakia. They also affect Poland and Hungary, but to a lesser extent because these countries are still able to benefit by transferring labor from agriculture to industry and have less difficulty in marketing their exports, an important part of which still consists of basic materials and foods. Rumania and Bulgaria, on the other hand, are still at a comparatively early stage of industrialization and, consequently, have plenty of reserves left.

Although basic factors made a slowdown inevitable, the extent of the slowdown in industry this year was due to some temporary factors. The extremely cold weather last winter caused substantial economic losses in the first quarter of 1963. Last year's bad harvest in several countries resulted in reduced production this year in the food-processing industry as well as in increased imports of foods, which competed with imports for industry. Because of balance-of-payments difficulties, East Germany, Czechoslovakia, and Poland planned to hold imports of industrial materials this year close to last year's level -- clearly a temporary expedient. East Germany and especially Czechoslovakia have cut down some unprofitable or unsaleable lines of production but have had difficulty in increasing production of goods that are profitable and in demand. In Czechoslovakia the frequent lowering of production

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goals and the attempts to change the structure of production have caused demoralization in factories and party echelons and exacerbated political conflicts, especially in Slovakia.

If the weather is more normal and if the regimes undertake strong reforms of economic management and show moderation and stability in economic policy, the Satellites should be able in the next few years to raise industrial production more rapidly than in 1963. But achievement of rates of growth of anything like the pre-1960 rate of about 10 percent appears to be out of the question except in Rumania and Bulgaria.

## 2. Continuation of Agricultural Difficulties

The stagnation of agricultural production, which began about 1960 in most of the Satellites, continued in 1963. On the basis of incomplete data it appears that total production in 1963 was near or below the 1959-62 average in all of the Satellites and that there was little or no increase above 1962 except in Rumania. Agricultural production in Poland probably dropped for the second year in a row, as a result of continued poor weather. The inefficiency of collective farms, as well as bad weather, is having adverse effects on agriculture in the other countries.

Production of grain in the Satellites as a group in 1963 was about the same as last year, but requirements for grain are slightly higher. Consequently, imports of grains also are slightly higher, and considerably larger amounts than the 1.6 million metric tons imported in 1962 are expected to come from the West because of the sharp drop in Soviet output of grain. Rumania, however, with good crops of corn and wheat in 1963, will be able to lend 400,000 metric tons of wheat to the USSR, as recently agreed to, while maintaining exports of corn to Western Europe at about the level of last year. Numbers of livestock and output of livestock products remained the same or declined this year in most Satellites because of the limited fodder supply.

## 3. Little Change for Consumers

The stagnation of agricultural production, especially of livestock products, has been the strongest influence on personal consumption in 1963. Supplies of quality foods, such as meat and dairy products, have remained at or slightly below last year's level in each country. Imports were increased or exports reduced to avoid sharp drops in supply in

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some countries. Purchases of soft goods, such as textiles, also have stagnated this year, because of consumer resistance to buying items of low quality, inflexible price and marketing policies, and restrictions on imports of such materials as wool and cotton. Supplies of consumer durables have continued to increase but still represent only a small part of consumer purchases.

Inflationary pressures have been less severe this year than in 1962 in East Germany and Czechoslovakia, mainly because of tight government controls over wages. In Poland, however, where employment and wages increased sharply during the spring and summer as a result of attempts to make up for last winter's losses, there is a good bit of excess purchasing power. Excess funds have gone mainly into savings deposits, but these constitute a potential source of inflationary pressure. The improvement in the balance between supply and demand in East Germany and Czechoslovakia removes in part what had been an acute irritant for the consumer -- the need to queue up for goods in stores. Nevertheless, popular dissatisfaction with living conditions continues to be high in both countries. In Poland, where dissatisfaction has increased this year, the probable lengthening of queues this winter may cause a further increase in dissatisfaction.

#### 4. Reduction in Investment Programs

Investment in the European Satellites in 1963 was hit hard by the disruptive effects of the cold winter on construction activity, by a slowdown in the growth of machinery production, and by the high priority given to exports. Mainly because of the slowdown in construction during the winter, investments fell sharply (or grew more slowly) in the first quarter of 1963 in all of the Satellites except Rumania, and subsequent efforts have not made up for the loss in construction work. Production of machinery may have declined in Czechoslovakia, and it increased more slowly than in 1962 in every other country except possibly Rumania. Difficulties in obtaining appropriate assortments of finished steel, in meeting the particular requirements of foreign customers, and in finding sufficient skilled labor were mainly responsible for this decline. In East Germany and Poland, exports of machinery were given priority over domestic investments and increased considerably, and there probably was also an increase in Czechoslovakia. Consequently, investments are expected to decline by about 10 percent in Czechoslovakia (following a 2.6-percent decline

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last year), to show almost no increase in East Germany for the third year in a row, and to increase much less than in 1962 in Poland.

The regimes in these countries have tried with limited success to maintain schedules for construction of key projects already underway -- such as the Friendship oil pipeline, the Kosice steel works in Czechoslovakia, and the Schwedt oil refinery in East Germany -- and to increase investments in agriculture. Less important industrial projects and housing construction have been delayed greatly, however, and new projects have been cut sharply. These lags and reductions are now extensive enough to reduce significantly the possibilities for industrial growth in the next few years, especially in East Germany and Czechoslovakia.

5. New Emphasis in Economic Policy on "Slack" Plans and Increased Efficiency

The new approach in economic policy in the European Satellites of drawing up "slack" instead of "taut" plans and of emphasizing efficiency, quality, and assortment instead of sheer quantity of output was given a further boost by developments in 1963. In East Germany, where economic plans for 1962 and 1963 were already fairly moderate, the plan for 1964 appears to be still more conservative. Czechoslovakia probably will set "slack" plans also for the next year or two, as it did in 1963. The new emphasis on efficiency and on "production for use, not for production's sake" in order to be effective requires that output be planned conservatively and probably entails some actual sacrifice, at least in the short term, in the volume of production. The East German and Czechoslovak regimes appear to be quite serious about the new emphasis, to the point that they are cutting out some lines of production and possibly are planning to shut down some inefficient plants.

The Poles and Hungarians also are shifting their attention to qualitative factors, but because of the simpler requirements and the greater flexibility at their lower level of economic development, they do not regard the need for improvements in this area with the same urgency as the Czechoslovaks and East Germans. Even the Bulgarians express concern, but their foremost interest continues to be the rapid building up of new industries. The Rumanians, as if to demonstrate their independence, appear to be quite satisfied with the policies of the past few years, which stress rapid and broad industrialization.

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6. Slow Progress But No Breakthroughs in Intra-Bloc Economic Cooperation

The increased concern for economic efficiency in the USSR and the more industrialized Satellites has been reflected also in attempts to increase economic cooperation through the Council for Mutual Economic Assistance (CEMA). Increased specialization, both within and across national boundaries, is to be one of the principal ways to increase efficiency. Moreover, the setting of "slack" economic plans makes it easier to establish reliable commitments for mutual deliveries of products. Since the Conference of June 1962 in Moscow, the CEMA members have strengthened the technical basis for intra-Bloc cooperation, the staff support for CEMA activities, and the execution of CEMA agreements. In addition, formation of a CEMA bank has been agreed on, and some concrete agreements (mainly bilateral) for joint investments and specialization have been signed. However, a Soviet attempt to change the basis of cooperation by the formation of a CEMA planning staff failed because of the threat that it posed to the national sovereignty of the Satellites. The Rumanians, in fact, not only flatly rejected the Soviet proposal but publicly maintained that cooperation must not impose any constraints on national economic policies. The position of Rumania on CEMA, like that country's internal economic policies, reflects its large opportunities for raising per capita output through broad industrial development and, consequently, its relatively low interest in increased specialization and efficiency in existing industries.

7. Improvement in Economic Management and Incentives -- an Unsolved Question

Although the regimes of the industrialized Satellites have now diagnosed their economic ills with greater accuracy and sophistication than a year or two ago, they are still groping for a cure. It is one thing to realize that the system of management and incentives has discouraged innovation and hindered efforts to satisfy users' needs and another to find a politically acceptable solution. Although there is general agreement throughout the Bloc as to what is desirable -- clearer lines of authority in state administration, a better informed Party apparatus, and a system of incentives that rewards efficiency -- there are wide differences of opinion, and much confusion, as to the relative importance and particular form of these objectives.

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Ulbricht and Novotny react to these problems by increasing the role of the Party in economic administration -- an approach that may neutralize the attempt to assign responsibility more clearly in the state hierarchy. Hungary, on the other hand, appears to be deemphasizing the Party's role in day-to-day economic administration so that its managerial reforms -- along the same general lines as in East Germany and Czechoslovakia -- may be more effective. The Polish regime seems concerned primarily with maintaining and, if possible, increasing its limited and uncertain authority over the economy and is coping with economic problems one by one, apparently without a general plan. The reforms in Bulgaria are nominally patterned after those in other Satellites and the USSR, but it is doubtful that there has actually been much change in the regime's approach to economic problems. Consistent with its policies in other respects, Rumania is leaving economic management about the way it is.

The desire to "improve" incentives is virtually universal in the Satellites, and even the East German regime is seriously considering proposals of basing bonuses on profitability. However, the regimes, for good reason, evidently are unwilling to allow very much scope for the operation of economic incentives and, in fact, have tightened central controls in most countries. Liberal economists, especially in Czechoslovakia, are pushing for much more extensive decentralization, even for a system similar to that of Yugoslavia, but the chances that such a solution will be adopted are slim, at least in the next few years.

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